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CHEMICAL

Financial Digest

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Analysis of Business Trends Plus Selected Financial Indicators

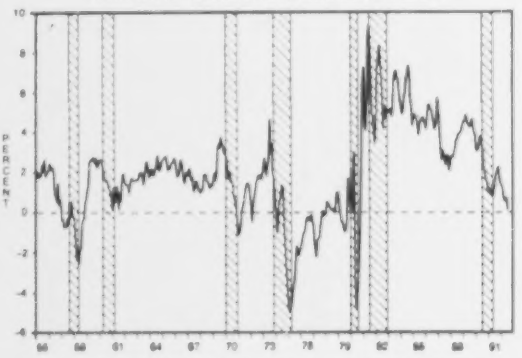
Monetary Policy Failings?

Although the dust has barely settled in the wake of the most recent easing of monetary policy earlier this month, the cottage industry of so-called "market watchers" is already urging the Federal Reserve to initiate the next round of interest rate cuts. To the critics, the measured pace of monetary ease over the past three years has been far too cautious to resuscitate the ailing economy. If the brakes on monetary policy had been lifted more aggressively, according to this view, M2 money supply growth would be faster, the inflation-adjusted Federal funds rate would be deeply riveted in negative territory and the demand for credit would be bounding higher, rather than treading water.

But while the monetary reins could have been loosened more quickly, it is doubtful whether or not the subsequent impact on the economy would have been any different than the results produced so far. For with consumers and businesses reluctant to borrow at almost any price, commercial banks tightening lending standards in response to regulator demands and balance sheet concerns, defense spending cuts extracting a hefty toll on employment, and diminished interest income pinching household spending, the health of this economy pivots around far more than the next one-half percentage point reduction in the Federal funds rate or another percentage point or two of money supply growth.

Perhaps the principal cause for concern at this juncture is the continuing anemic growth of both money and credit—two of the lubricants which tend to power economic activity. The growth of the M2 money supply, for example, has been stuck in low gear all year long, rising by a paltry 1½ percent so far this year, or well below the Federal Reserve's 2½ to 6½ percent target range. Even more noticeable has been the virtual absence of the usual post-recession wave of private sector borrowing and spending, which in the past has satisfied the pent-up demands for new homes and automobiles or provided the wherewithal for business spending on new plant and equipment. Over the past year, potential borrowers have largely turned a blind eye toward the drop in interest rates; private sector debt outstanding has risen by just two percent. Although this may seem like a fair-sized, if modest number, it pales in comparison with the past and is actually less than one-quarter of the rate of rise in private sector credit typically experienced during the initial stages of recovery from preceding post-war recessions.

SPREAD BETWEEN FEDERAL FUNDS RATE AND 12-MONTH PERCENT CHANGE IN TOTAL CPI



Source: Federal Reserve Bank of NY, Bureau of Labor Statistics

For the pundits to point out the dearth of money and credit growth is one thing, but to attribute them to monetary policy failings is quite another. The lackluster pace of M2 growth can be directly traced not to the central bank, but to the unwillingness of consumers to rollover small-saver certificates of deposit at interest rates now approaching thirty-year lows. Rather than symptomatic of a liquidity-starved economy, the deficiency in M2 growth this year reflects both the increasing financial sophistication of many small savers and the multitude of financial products, many of which lie outside the traditional components of the money supply, competing for small-saver dollars. The growth of the M1 money supply, in contrast, which has been far less affected by the tidal wave of deposit shifts now underway and provides a better gauge of transactions-related liquidity, has not only been expanding at a much more vigorous clip than M2—nearly 13 percent so far this year—but at a pace which some fear is far too robust if price stability is to be maintained.

Credit Malaise

Nonetheless, hardly anyone suggests that the Fed should lift interest rates in order to prompt a reflow of funds into small certificates of deposit, and thereby have a better shot at achieving this year's M2 target. So, too, policy remedies for the credit malaise have proven

Economics Department 44/270

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clusive. For notwithstanding the Fed's increasingly generous provision of nonborrowed reserves to the banking system—the wherewithal to turn on the credit spigot—the results have been disappointing. Short-term commercial and industrial loan demand has been easing for months, consumers have been attempting to lighten debt burdens and banks have been striving to meet stricter capital standards. If all this seems like a recipe for a borrowing and lending torpor, it is; with private borrowers scarce, banks have been lending to the Federal government, increasing their purchases of Treasury securities by more than 20 percent over the past year.

But even a relaxation of regulatory standards, as some suggest, will have only a modest impact on loan demand if borrowers remain on strike. And, in the absence of simply giving money away, the only other alternative is to do just about that, namely, drive short-term interest rates well below the rate of inflation. However, even reducing the "real" cost of money far below zero might not be a magic bullet for the economy. As shown in the chart, although the inflation-adjusted Federal funds rate does, indeed, stand well above the rate prevailing at the trough of most other recessions, it has been falling for months with little effect and, at its present level, can hardly be considered a signifi-

Short Term Paper Outstanding

(Millions of Dollars)

Time Deposits $100,000 or more Weekly Reporting Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (9/2/92)	134,754	- 756	- 49,420
New York City (9/9/92)	25,199	+ 10	- 4,785
Commercial Paper (9/9/92)	542,430	+ 1,054	+ 12,443

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (9/2/92)	275,956	+ 960	- 24,001
New York City (9/9/92)	47,459	- 774	- 6,423

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (9/2/92)	987,232	+ 3,928	- 30,180
New York City (9/9/92)	157,815	- 2,229	- 10,582

Financial Markets

	Friday 9/18/92	Change Since Week Ago	Change Since Year Ago
U.S. Governments, 2 p.m. Yields:			
90-Day Bills†	2.94%	- .02	- 2.37
180-Day Bills†	2.99	- .02	- 2.45
Longest Bills†	3.13	- .02	- 2.41
Recent Issues:			
4¼s 8/31/94	3.82	- .01	
5⅛s 8/31/97	5.39	+ .09	
6⅜s 8/31/02	6.41	+ .07	
7½s 8/31/22	7.35	+ .07	
Municipals:			
Bond Buyer—20 Bond Index* (9/17/92)	6.27%	+ .11	- .51
Blue List Total ($ Million)	$ 1,268	+ $ 306	- $ 115
30-Day Visible Supply ($ Million)	$ 9,214	+ $3,986	+$5,477
Total	$10,482	+ $4,292	+$5,362
Corporates:			
Moody's Aa Composite (9/17/92)	8.16%	+ .05	- .69
30-Day Visible Supply ($ Million)	$ 2,030	- $ 255	+$1,415
Stocks: (Thursday)			
Dow-Jones Averages:			
Industrials	3,327.03	+ 21.33	+307.80
Transportation	1,286.64	+ 9.05	+ 99.40
Utilities	220.33	- 1.5	+ 12.15
65 Stocks	1,166.64	+ 5.29	+ 96.03
N.Y.S.E. Composite Index	232.39	+ 1.59	+ 19.41
N.Y.S.E. Avg. Daily Vol. for Week (000's)	243,451	+ 58,225	+56,603

*34% Taxable equivalent 9.50%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 9/18/92	Week Ago
Overnight	3.06%	3.06%
1 month	3.25	3.25
3 month	3.25	3.19
6 month	3.31	3.25
1 year	3.44	3.38

FOREIGN EXCHANGE SPOT RATES

New York Opening (9/18/92)	Currency Per U.S. $	Week Ago
Belgium	31.00	29.55
Canada	1.2213	1.2231
France	5.1250	4.8674
Germany	1.4977	1.4347
Italy	1260.08	1097.02
Japan	124.53	123.48
Mexico	3091.01	3063.00
Netherlands	1.6674	1.6000
South Korea	785.95	784.40
Switzerland	1.2994	1.2870
Taiwan	25.04	24.94
U.K.*	1.7475	1.9465

*U.S. $ per U.K. pound

CHEM TRADE-WEIGHTED DOLLAR (9/18/92) (Adjusted for Inflation)	Change Since Week Ago	Change Since 2/27/85
	+5.4%	-18.1%

cant impediment to recovery. The real Federal funds rate stood at nearly five percentage points at the trough of the 1981-82 downturn, yet the economy was soon to embark on the longest peacetime expansion in history.

Pushing On A String

With M1 money supply growth running in the double-digits, the banking system awash with nonborrowed reserves and short-term interest rates plumbing ever-lower depths, the Federal Reserve is rapidly approaching the point at which it will find itself "pushing on a string"—when, despite its best efforts, monetary policy will have done all it can do to jump-start the economy. As a consequence, the critics' gaze will of necessity shift from the presumed policy shortcomings of the Fed to the true culprits behind today's business lethargy. Although the list is lengthy, they include sharp reductions in defense-related procurement, the erosion of corporate profitability, the Tax Act of 1986, which sapped the muscle of commercial construction and the hefty tax increases which accompanied the Deficit Reduction Act of 1990. Until these obstacles are either overcome, or their influence wanes, the effectiveness of even the best-intentioned, and well-executed monetary initiatives will be blunted, and subpar growth will persist. ///

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 9/16/92	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	290.365	+ 1.638	+23.315
Loans to Depository Inst.	426	+ .212	- .436
Float	1.039	+ .748	+ .414
Total Reserve Bank Credit	323.656	+ 2.864	+23.783
Treasury Deposits with Federal Reserve Banks	6.284	+ .361	- 2.037
Currency in Circulation	320.003	+ .546	+25.023
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	291.497	- 2.935	+39.848
	9/16/92		
Member Bank Reserves:			
Total Reserves Held	51.427	+ 1.897	- .751
Excess (Deficiency)	.681	- .381	- .051
Net Free Reserves	.361	- .443	- .039
Monetary Aggregates †		**‡ % Change Since 3 Months Ago***	**% Change Since Year Ago**
M1 (9/7/92)	983.3	+ 9.5	+ 12.5
M2 (9/7/92)	3.477.3	+ 0.5	+ 1.7
M3 (9/7/92)	4.172.8	+ 0.1	+ 0.3
Domestic Nonfinancial Debt (1st Q'92)	11.304.3	+ 3.9	+ 4.5

† Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 9/4/92	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	2.89%	2.91%	3.02%
* Federal Agencies	3.05	3.05	3.20
* Municipal Notes–High Grade (34% Taxable Equivalent)	4.39	4.55	4.62
Negotiable Time CDs Chemical	Rates By Arrangement		
* Secondary Market–Prime	3.10	3.15	3.35

‡ Finance Company Paper–Prime	
5- 14 days	3.10%
15- 29 days	3.10
30- 59 days	3.08
60- 89 days	3.05
90-179 days	3.00
180-239 days	3.05
240-270 days	3.08

‡* Bankers' Acceptances	
Oct.	3.04%
Nov.	3.01
Dec.	3.01
Jan.	3.05
Feb.	3.03
Mar.	3.03

‡ Industrial Paper–Prime	
30- 89 days	3.10%
90-120 days	3.10

†Federal Funds Effective Rate	3.00%

‡ Discount basis. *Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross Domestic Product (Current Dollars)*	2nd Q'92	$ 5,899	$ 5,840	$ 5,658
Gross Domestic Product (1987 Dollars)*	2nd Q'92	$ 4,891	$ 4,874	$ 4,817
Percent Change, Annual Rate	2nd Q'92	1.4	2.9	1.7
Change in Consumer Prices*	Aug '92 n	3.6%	1.2%	3.6%
Change in CHEM Cost of Living Index*	Aug '92 n	6.0%	1.2%	4.8%
Change in Producer Prices*	Aug '92 n	1.2%	1.2%	2.4%
Civilian Employment (Thousands of Persons) †	Aug '92	117,737	117,772	116,484
Unemployment as % of Civilian Labor Force †	Aug '92	7.6%	7.7%	6.8%
Personal Income*	Jul '92	$ 5,050	$ 5,039	$ 4,828
Leading Indicators Composite Index (1967=100) †	Jul '92	149.6	149.5	145.6
Industrial Production Index (1977=100) †	Aug '92 n	108.6	109.2r	108.0
Net Change in Consumer Installment Credit †	Jul '92 n	- $ 1.12	- $ 0.28r	- $ 1.29
U.S. Merchandise Trade Balance †	Jul '92 n	- $ 7.82	- $ 6.73r	- $ 5.63
Plant and Equipment Expenditures*	4th Q'92 n	$ 562.4 (a)	$ 565.2 (a) r	$ 528.9
Private Housing Starts (Thousands of Units)*	Jul '92	1,119	1,151	1,053
New Construction Expenditures*	Jul '92	$ 422.0	$ 424.4	$ 397.0
Total Business Inventories †	Jul '92 n	$ 832.9	$ 831.9r	$ 819.9r
Total Business Sales †	Jul '92 n	$ 558.5	$ 554.4r	$ 538.9r

*Seasonally adjusted annual rate. † Seasonally adjusted. n-Newly reported figure r-Revised. a-Anticipated.

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